

Lease agreements that contain purchase options equal to the fair market value of the tangible personal property at the end of the lease term are considered true leases, and the lessors incur Use Tax liability on their cost price of tangible personal property purchased for rental purposes. See 86 Ill. Adm. Code 130.2010. (This is a GIL).

February 25, 2000

Dear Xxxxx:

This letter is in response to your letter dated December 20, 1999 that we received on January 13, 2000. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

COMPANY is a leasing company which enters into long term leases of tangible personal property in your state and is registered for sales tax purposes. Please opine on the following:

- 1) We sell a lease to another Lessor, yet as a service to the new Lessor we continue to bill the Lessee for rentals and sales taxes, and remit the sales tax to the taxing authorities on our tax return; is this acceptable?
- 2) We sell the receivable only to another Lessor, and we retain title and rights to any residual. Which party is legally responsible for billing and remitting of sales taxes? Is it all right for us to handle this function?
- 3) We are considering entering into a new business in which we would provide a service to another leasing company under which we will bill and collect rentals and sales taxes and remit to the proper taxing authority on our own tax returns for their leases. Is this acceptable?
- 4) We sell a Lease to another Lessor who is not registered for sales tax purposes in your taxing jurisdiction. This transaction is the only business this other leasing company does in your locality. Does this Lessor need to register for sales tax purposes, or is it okay for him to not register and instead have us act as his Agent for the purposes of billing, collecting and remitting sales taxes?
- 5) We enter into a partnership with another Leasing Company. Each party contributes Leases into the partnership in exchange for partnership interest. Does the

partnership have to be registered for sales tax purposes or is it okay for one of the partners, who is already registered, to bill, collect and remit sales taxes under its own registration number?

Thank you for your assistance.

For general informational purposes we enclose a copy of 86 Ill. Adm. Code 130.2010, the Department's regulation that covers the taxation of leases. Although your questions presume that rental receipts are subject to sales tax, that is generally not true in Illinois for rental payments received pursuant to true leases. Under Illinois law, "true leases" and "leases" that are actually conditional sales contracts are treated differently for Retailers' Occupation and Use Tax purposes. Lessors are subjected to a Use Tax on their cost price of tangible personal property that they acquire to use by leasing under true leases in Illinois. This means lessors in Illinois encounter a front-end tax on value rather than an amortized tax on receipts. The only exception is automobiles rented for one year or less, which are subject to the Automobile Renting and Use Tax found at 35 ILCS 155/1 et seq.

True leases generally have no buy out provisions at the close of the leases. If buy out provisions do exist, they must be fair market value buy out options in order to maintain the character of the true leases. Lessors of tangible personal property under true leases in Illinois are deemed end users of the property to be leased. See, 86 Ill. Adm. Code 130.220(a). As end users of tangible personal property located in Illinois, lessors incur Use Tax liability on their cost price of such property. Except for short-term automobile rentals, there is no tax due upon rental receipts in Illinois.

Under Section 130.2010(a), persons who purport to "lease" the use of property, but in fact sell such tangible personal property to nominal "lessees," are considered to be making conditional sales subject to Retailers' Occupation Tax. Such would be the case when the agreements contain nominal purchase options at the end of the lease term. In these situations Retailers' Occupation Tax is due on all the payments received by the "lessors." Interest or finance charges may be excluded from gross receipts if the books of the retailers ("lessors") clearly reflect the amounts of the payments attributable to financing. See 86 Ill. Adm. Code 130.420, enclosed.

Under Illinois law, lessors may not "pass through" their Use Tax obligation to lessees as taxes. However, lessors and lessees may make private contractual arrangements for a reimbursement of the tax to be paid by the lessees. If lessors and lessees have made private agreements where lessees agree to reimburse lessors for the amount of the tax paid, then lessees are obligated to fulfill the terms of the private contractual agreements.

Where persons sell tangible personal property that is encumbered by a lease and purchasers assume all rights, title, and interest in the lease agreements, such sales are sales at retail whose receipts are subject to Illinois Retailers' Occupation Tax. A portion of the sale proceeds may represent an intangible, that of future lease receivables. However, a deduction of this intangible portion of the sales receipts is only authorized when the books and records of sellers accurately

document these intangible amounts. Absent this documentation, the entire proceeds would be subject to tax. See, 86 Ill. Adm. Code 130.220(c), enclosed.

Where persons sell intangibles only, such as receivables, there are no Illinois Retailers' Occupation/Use Tax consequences because there has been no exchange of tangible personal property for consideration. This can occur in lease situations if the title to the lease assets is not transferred, but the lease receivables are sold.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Karl W. Betz
Associate Counsel

KWB:msk
Enc.